Fiscal Note 2017 Biennium

Bill #	SB0157	**Title:**	Generally revise tax reappraisal laws
Primary Sponsor:	Tutvedt, Bruce	**Status:**	As Amended in Senate Committee

- [x] Significant Local Gov Impact
- [x] Needs to be included in HB 2
- [ ] Technical Concerns
- [ ] Included in the Executive Budget
- [ ] Significant Long-Term Impacts
- [ ] Dedicated Revenue Form Attached

FISCAL SUMMARY

	FY 2016 Difference	FY 2017 Difference	FY 2018 Difference	FY 2019 Difference
Expenditures:				
General Fund	($289,592)	$153,177	$980,421	$972,569
Revenue:				
General Fund	$11,739,500	$9,919,500	$7,929,500	$5,779,500
State Special Revenue	$734,335	$624,335	$494,335	$364,335
Net Impact-General Fund Balance:	$12,029,092	$9,766,323	$6,949,079	$4,806,931

Description of fiscal impact: SB 157, as amended, revises property tax laws by changing the reappraisal cycle from a six-year cycle to a two-year cycle; adjusting the rates at which the market value of property is taxed to maintain taxable value neutrality between residential, agricultural, commercial, and timber properties on a statewide basis; extending the base period of the data for the valuation of forest land; and revises the property tax assistance programs to allow for more incremental assistance based on income. The changes in taxable value under this bill create a guaranteed tax base aid (GTB) savings beginning in FY 2016. This bill is effective on passage and approval and applies retroactively to TY 2015.

FISCAL ANALYSIS

Assumptions:

Department of Revenue

1. Under current law, the increase in reappraisal value for class 3 agricultural land, class 4 residential and commercial real property, and class 10 forestland is phased-in over six years. However, if a property decreased in value, the new (lower) value is applied in the first year. For each year over the six years, the

homestead exemption for class 4 residential real properties would remain at 47% and the comstead exemption for class 4 commercial properties would remain at 21.5%. The tax rate for classes 3 and 4 would be 2.47% and the tax rate for class 10 would be 0.29%.

2. SB 157 proposes two principle things: 1) move reappraisal from a six-year cycle to a two-year cycle, and 2) implement a policy of taxable value neutrality on a statewide basis for agricultural, residential, commercial, and timber properties. That is, SB 157 sets the tax rates so that the overall taxable value for these types of properties stays the same on a statewide basis.

Calculation of taxable value neutrality by class

3. The change in value for agricultural land is predominantly determined by the changes in commodity price used to determine productivity value for the land.
4. Forest land values are determined by the University of Montana, College of Forestry and Conservation productivity estimates with input from the timber industry.
5. Under current law, timber values are determined using a five-year price average, and a capitalization rate of 8%.
6. Under the provisions of the amended version of SB 157, forest land is valued using a ten-year average price and a capitalization rate of 6.4%.
7. The market value for residential and commercial properties is determined by using the sales, cost, or income approach to valuation.
8. The following table shows relevant information about the changes in value on a statewide basis for the different types of property over the six-year cycle.

	Estimated Change in Value	
Type of Property	Current Law	SB 157 as amended
Residential	-2.85%	-2.85%
Commercial	2.45%	2.45%
Agricultural	16.72%	16.72%
Forestland	-50.22%	-21.29%

9. Although current law sets the tax rate at 2.47% for agricultural, residential, and commercial property, because of the homestead and comstead exemptions, the actual rate is for these classes of property is equal to 2.47% multiplied by the exemption rates.
10. For the majority of residential properties, the rate used to determine taxable value is equal to the statutory rate times one minus the homestead exemption percentage, or 1.31% (2.47% X (100% - 47%)). The exemption does not apply to a single-family dwelling value over $1.5 million. The rate is equal to 2.47% for the value above $1.5 million.
11. Under current law, the rate used to calculate taxable value for commercial property was equal to the statutory rate multiplied by one minus the comstead exemption or 1.94% (2.47% X (100% - 21.5%))
12. The following table displays these rates for agricultural, residential, and commercial:

Agricultural, Residential, and Commercial Property Tax Rates

Property Type	Rate	Exemption Rate	Actual Rate
Agricultural	2.47%	0.00%	2.47%
Residential	2.47%	47.00%	1.31%
Commercial	2.47%	21.50%	1.94%

13. A policy of taxable value neutrality on a statewide basis for agricultural, residential, commercial, and timber properties would set the rates so that the overall taxable value for these types of properties stayed the same on a statewide basis between TY 2014 and TY 2015.

14. If all agricultural land was taxed the same, the taxable value neutral rate would be equal to the TY 2014 taxable value divided by the TY 2015 market value. However, non-qualified agricultural property is taxed at a rate equal to 7 times the statutory agricultural rate (15-6-433(3), MCA). Therefore, to calculate a taxable value neutral rate, the TY 2014 taxable value needs to be divided by the market value of the qualified agricultural properties, and seven times the market value of the non-qualified properties. This relationship is presented in the following equation:

$$Tax\ Neutral\ Rate = \frac{Taxable\ Value_{TY14}}{Qual.Market\ Value_{TY15} + 7(Non - Qual.Market\ Value_{TY15})}$$

15. Total agricultural taxable value in TY 2014 was equal to $143.897 million. The market value for qualified agricultural properties after reappraisal is equal to $6,336.489 million and the market value for non-qualified agricultural property is equal to $45.061 million. If we substitute these values into the previous equation we get the following:

$$Tax\ Neutral\ Rate = \frac{\$143{,}896{,}608}{\$6{,}336{,}489{,}328 + 7(45{,}061{,}332)}$$

$$Tax\ Neutral\ Rate = \frac{\$143{,}896{,}608}{\$6{,}651{,}918{,}652}$$

$$Tax\ Neutral\ Rate = 2.1632\%$$

16. The taxable value neutral rate for commercial and residential properties faces similar and more numerous deviations from the statutory rates. Because of the numerous rate variations, a display of the calculation of the taxable value neutral rate would be impractical.
17. The relative proportion of value for properties where the actual rate deviates from the rates defined explicitly in code are much smaller.
18. As a result of the previous two assumptions, the taxable value neutral rates will deviate from simply dividing the TY 2014 taxable value by the new market value, but the deviation is of a much smaller magnitude relative to the deviation in the taxable value neutral agricultural rate.
19. Unlike agricultural, residential, and commercial properties, there are currently no deviations from the primary rate of class 10 properties. As a result, the stated rate and the effective rate for class ten are equal to each other.
20. The following table shows the TY 2014 market value, taxable value, and effective rates for the different classes of property. For TY 2015, the new market values are displayed along with the TY 2014 taxable values, and new taxable value neutral effective tax rates are calculated.

Taxable Value Neutral Calculations
($ Millions)

Agricultural Property

	TY 2014		TY 2015
Market Value (Given)	$5,467.386		$6,381.551
Effective Rate*	x 2.63%		x 2.25%
Taxable Value	$143.897	→	$143.897

Commercial Property

	TY 2014		TY 2015
Market Value (Given)	$18,294.152		$18,742.568
Effective Rate*	x 1.92%		x 1.87%
Taxable Value	$350.605	→	$350.605

Residential Property

	TY 2014		TY 2015
Market Value (Given)	$89,778.076		$87,218.359
Effective Rate*	x 1.30%		x 1.34%
Taxable Value	$1,168.360	→	$1,168.360

Timber Property

	TY 2014		TY 2015
Market Value (Given)	$2,155.929		$1,696.921
Effective Rate*	x 0.29%		x 0.37%
Taxable Value	$6.252	→	$6.252

*Effective rates differ from statutory rates as a result of different rates for properties in the same tax class. Non-qualified agricultural land and golf courses are examples.

Setting taxable value neutral tax rates by class

21. Section 5 of the bill changes the rate from 2.47% to 2.16% for agricultural land.
22. SB 157 eliminates the homestead exemption and changes the rate from 2.47% to 1.35% for all residential property value except the value of single-family dwellings over $1.5 million, which has a rate of 1.44 times the regular residential rate, or 1.944% (i.e. the equivalent to having a statutory rate equal to the new class four commercial rate).
23. SB 157 eliminates the comestead exemption and changes the rate to 1.44 times the residential rate of 1.35%, or 1.944%.
24. SB 157 changes the rate used to determine taxable value for forestland from 0.29% to 0.37%.

Accounting fora two-year reappraisal cycle

25. Under current law, the market value for property that increased in value between 2002 and 2014 will be phased in by one-sixth increments over the reappraisal cycle ending in 2020. However, if property values decrease, then the decreased market value is not phased in. SB 157 proposes to remove phase-in so that all changes in value will occur in the first year, both positive and negative, and move to a two-year cycle.
26. The table below shows the estimated proportion of properties in each tax class that have increased, decreased, and stayed the same:

Property	Increased in value	Decreased in Value	No Change	Total
Residential	51.2%	48.4%	0.3%	100%
Commercial	51.3%	48.0%	0.7%	100%
Agricultural	27.6%	72.4%	0.0%	100%
Forestland	0.0%	100.0%	0.0%	100%

27. Estimated changes from HJR 2 for FY 15, FY 16 and FY 17, and Office of Budget and Program Planning for FY 18 and FY 19, for the different types of property were applied. The following table shows the estimated current law taxable value, estimated SB 157 taxable value, and the change in taxable value as a result of SB 157 in millions of dollars.

Fiscal Year	Agricultural	Residential	Commercial	Timber	Total
Current Law Taxable Value ($ million)					
FY 2015	$143.9	$1,168.4	$350.6	$6.3	$1,669.1
FY 2016	$136.0	$1,077.1	$331.5	$3.1	$1,547.7
FY 2017	$147.2	$1,129.5	$350.0	$3.1	$1,629.8
FY 2018	$159.1	$1,184.7	$369.4	$3.1	$1,716.3
FY 2019	$171.8	$1,242.7	$389.8	$3.0	$1,807.3
Taxable Valuse SB 157 ($ million)					
FY 2015	$143.9	$1,168.4	$350.6	$6.3	$1,669.1
FY 2016	$143.7	$1,162.0	$359.4	$6.3	$1,671.4
FY 2017	$149.3	$1,205.6	$373.2	$6.3	$1,734.4
FY 2018	$155.2	$1,251.2	$387.5	$6.2	$1,800.1
FY 2019	$161.3	$1,298.7	$402.4	$6.1	$1,868.6
Change in Taxable value ($ million)					
FY 2015	$0.0	$0.0	$0.0	$0.0	$0.0
FY 2016	$7.7	$84.9	$27.8	$3.2	$123.7
FY 2017	$2.1	$76.1	$23.2	$3.2	$104.6
FY 2018	($3.9)	$66.5	$18.1	$3.2	$83.8
FY 2019	($10.4)	$56.0	$12.6	$3.1	$61.3

28. The state mills were then applied to the change in taxable value to determine the estimated fiscal impact to the state. All property is levied the university mills (6) and the school equalization mills (95). Property in Silver-Bow, Cascade, Yellowstone, Missoula, and Lewis & Clark are levied additional Vo-Tech mills (1.5). The following table shows the estimated fiscal impact to the state of SB 157.

Estimated Change in State Property Tax Revenue
(Millions $)

Fiscal Year	General Fund	University Mills	Total
FY 2016	$11.83	$0.74	$12.58
FY 2017	$10.01	$0.63	$10.64
FY 2018	$8.02	$0.50	$8.53
FY 2019	$5.87	$0.37	$6.24

<u>*Property Tax Assistance (PTAP) and Montana Disable Veterans (MDV) Programs*</u>

29. SB 157 also adjusts the Property Tax Assistance Program (PTAP) and the Montana Disabled Veterans (MDV) program. Under current law, income brackets are used to determine the amount of property tax assistance for both the PTAP and MDV programs. Current law sets a $100,000 taxable market value limit to the PTAP program. Finally, current law requires the PTAP and MDV programs to update their income thresholds each year based on a Personal Consumption Expenditure (PCE) price index. Under the provisions in SB 157, the income brackets used to determine the amount of PTAP or MDV assistance are eliminated and replaced with a formula based on income to avoid large changes in assistance caused by moving between brackets from one year to the next, due to small changes in income. The formula to be used will be administered by the department through rulemaking authority and updated on an annual basis to account for inflation. SB 157 replaces the $100,000 taxable market value limit in the PTAP program with a $170,000 appraised value limit. The PCE index is replaced with a Consumer Price Index (CPI) inflation adjustment factor in SB 157.
30. By comparing the impacts SB 157 would have had on a sample of PTAP and MDV applicants in TY 2014 relative to current law, it is estimated the elimination of the stepped income brackets, $100,000 limit in

taxable market value, change in price indexes, and modified tax rates to the PTAP and MDV programs will reduce general fund property tax revenue by approximately $90,500 per year and University property tax revenue by $5,665 per year.

31. SB 157 eliminates Extended Property Tax Assistance Program (EPTAP). To qualify under current law, a property owner must have had an increase in value of more than 25% as a result of 2008 reappraisal and have an increase in tax liability of more than $250 in 2008. However, because of the statutory language in 15-6-193 MCA, taxpayers would have a lower taxable value if they chose not to participate in EPTAP, assuming they qualified. Therefore, the estimated impact of eliminating EPTAP is expected to be negligible.

Department Costs

32. Implementation of SB 157 is expected to require an additional 11.00 FTE in the Property Assessment Division (PAD) and an additional 1.00 FTE in the Business and Income Tax (BIT) division. Expenses are estimated to be approximately $0.689 million per fiscal year for personal services, approximately $0.301 per fiscal year for operating expenses, approximately $0.039 million in one-time operating costs. It is assumed that these costs will be funded from the general fund.

Office of Public Instruction

33. Local school district mills would shift among tax types to provide the necessary revenue for school district budgets. The amount each taxpayer pays will change based on the change in value of property with respect to the district average but total local school taxes paid would essentially match present law.
34. The changes SB 157 proposed for property tax creates a net GTB savings for the state. The general fund savings are outlined below:

FY 2016	FY 2017	FY 2018	FY 2019
($1,300,224)	($836,127)	($18,890)	($28,057)

35. Changes to property tax values may have an impact on the Natural Resource Development (NRD) K-12 Payment. However, the changes in this bill are not expected to cause a significant fiscal effect to the NRD payments.
36. Revenue received from county school levies for all district funds will not change due to this bill as tax shifting occurs.
37. The shift of tax liability occurs between tax classes, but results in negligible change to retirement GTB.

Fiscal Impact:	**FY 2016 Difference**	**FY 2017 Difference**	**FY 2018 Difference**	**FY 2019 Difference**
Department of Revenue				
FTE	12.00	12.00	12.00	12.00
Expenditures:				
Department of Revenue				
Personal Services	$681,036	$681,056	$692,151	$703,442
Operating Expenses	$329,596	$308,248	$307,160	$297,184
Office of Public Instruction				
Local Assistance (GTB)	($1,300,224)	($836,127)	($18,890)	($28,057)
TOTAL Expenditures	($289,592)	$153,177	$980,421	$972,569
Funding of Expenditures:				
General Fund (01)	($289,592)	$153,177	$980,421	$972,569
TOTAL Funding of Exp.	($289,592)	$153,177	$980,421	$972,569
Department of Revenue				
Revenues:				
General Fund (01)	$11,739,500	$9,919,500	$7,929,500	$5,779,500
State Special Revenue (02)	$734,335	$624,335	$494,335	$364,335
TOTAL Revenues	$12,473,835	$10,543,835	$8,423,835	$6,143,835
Net Impact to Fund Balance (Revenue minus Funding of Expenditures):				
General Fund (01)	$12,029,092	$9,766,323	$6,949,079	$4,806,931
State Special Revenue (02)	$734,335	$624,335	$494,335	$364,335

Effect on County or Other Local Revenues or Expenditures:

Department of Revenue

1. Local governments will see the same decreases from current law taxable value. However, since local government mill levies are set on current year taxable values, and revenue governed by 15-10-420, MCA, local mill levies will adjust to generate the required property tax revenue.

Office of Public Instruction

2. Local property taxes to support the school district BASE budgets may increase by approximately $1,294,621 in FY 2016, $843,799 in FY 2017, $20,135 in FY 2018, and $37,133 in FY 2019.

Sponsor's Initials	*Date*	*Budget Director's Initials*	*Date*